

BEFORE
THE PUBLIC SERVICE COMMISSION
OF SOUTH CAROLINA
DOCKET NO. 2004-297-S – ORDER NO. 2005-168
APRIL 6, 2005

IN RE:	Application of Midlands Utility, Inc. for)	ORDER GRANTING
	Approval of New Schedule of Rates and)	INCREASE IN RATES
	Charges for Sewerage Service Provided to its)	AND CHARGES
	Customers in Richland, Lexington, Fairfield)	
	and Orangeburg Counties.)	

INTRODUCTION

This matter comes before the Public Service Commission of South Carolina (“the Commission”) on an Application for increases in sewer rates and charges filed by Midlands Utility, Inc. (“Midlands” or “MUI”). Midlands’ Application was accepted by the Commission pursuant to S.C. Code Ann. § 58-5-210 *et. seq.* and 26 S.C. Code Regs. 103-512. Midlands’ Application was filed on October 6, 2004.

By correspondence, the Commission instructed Midlands to publish a prepared Notice of Filing, one time, in a newspaper of general circulation in the areas affected by Midlands’ Application. The Notice of Filing indicated the nature of the Application and advised all interested persons desiring to participate in the scheduled proceedings of the manner and time in which to file appropriate pleadings for inclusion in the proceedings. In the same correspondence, the Commission also instructed Midlands to notify each customer affected by the Application by mailing each customer a copy of the Notice of Filing. Midlands furnished the Commission with an Affidavit of Publication

demonstrating that the Notice of Filing had been duly published and with a letter in which Midlands certified compliance with the instruction of the Commission to mail a copy of the Notice of Filing to all customers affected by the Application. No Petitions to Intervene were filed.

The Office of Regulatory Staff made on site investigations of Midlands' facilities, audited Midlands' books and records, and gathered other detailed information concerning Midlands' operations. Prior to January 1, 2005, the Public Service Commission Staff also made on-site investigations.

On February 24, 2005 at 10:30 a.m., a public hearing concerning the matters asserted in Midlands' Application was held in the Commission's hearing room located at Synergy Business Park, 101 Executive Center Drive – Saluda Building, Columbia, SC. The full Commission, with Chairman Randy Mitchell presiding, heard the matter of Midlands' application. Scott Elliott, Esquire and Charles Cook, Esquire represented Midlands Utilities, Inc. Florence Belser, General Counsel of ORS and Wendy Cartledge, Esquire represented the Office of Regulatory Staff. David Butler, Esquire served as legal counsel to the Commission.

Midlands presented the testimony of Keith G. Parnell, President and Operations Manager of Midlands, and C. Kenneth (Ken) Parnell, Vice-President of Midlands and President of HPG and Company. The Office of Regulatory Staff presented testimony of Willie J. Morgan, Program Manager for the Office of Regulatory Staff Water and Wastewater Department, Dawn Hipp, Project Specialist for the Office of Regulatory Staff

Water and Wastewater Department, and Roy Barnette, Office of Regulatory Staff Auditor.

BACKGROUND AND PROCEDURAL MATTERS

Midlands is a closely held corporation organized and existing under the laws of the State of South Carolina and is a public utility within the meaning of S.C. Code Ann. §58-5-10(3) (Supp 2004). Midlands currently furnishes sewer collection and sewer treatment service to approximately 3,000 active residential and commercial customers in Richland, Lexington, Fairfield and Orangeburg Counties under the schedule of rates approved by the Commission in Order No. 97-517, Docket No. 96-160-S, dated June 17, 1997. By Commission Order No. 2002-138 in Docket No. 2001-380-S dated March 1, 2002, Midlands' approved schedule of rates includes a collection only residential sewer charge.

Midlands requested approval of a two step (or two phase) schedule of rates and charges for sewerage service provided to its residential and commercial customers in all areas served. The two step schedule of rates and charges would be implemented in two stages. Notice of Midlands' intention to file the new schedules was given more than the required thirty (30) days prior to this application. The first increase is required to raise rates to pay for new costs created by necessary construction of capital improvements. The second increase in rates will be required upon completion of construction.

Midlands and two other closely held corporations, namely Bush River Utilities, Inc. ("Bush River") and Development Services, Inc. ("DSI"), are all owned and operated by two brothers, Keith G. Parnell and C. Kenneth (Ken) Parnell, each owning equal

shares of these three family owned corporations. The corporations are connected by virtue of ownership, common purpose, staffing, and inter-company borrowings of assets and equipment. Each of the three corporations is a public utility within the meaning of S.C. Code Ann. §58-5-10(3) (Supp. 2004), and is therefore regulated by the Commission.

At the outset of the hearing, counsel for ORS and counsel for Midlands advised the Commission that the parties had reached an agreement with respect to certain issues in these matters. Scott Elliott, attorney for Midlands, advised the Commission that Midlands had already begun changing some of its business practices as a result of the recommendations of ORS. Mr. Elliott informed the Commission that Midlands has upgraded its billing form to reflect that the bill clearly states office hours, the phone number for emergency calls as well as routine calls and that Midlands has also submitted an updated authorized utility representative form. Mr. Elliott further stated that Midlands would follow the recommendations of ORS with respect to disconnect charges and interest rates to be charged on deposits and that Midlands desires to comply with the rules and regulations of the Commission.

Florence P. Belser, ORS General Counsel, advised the Commission that ORS does not contest the second phase of the increase going into effect provided that the Commission requires that ORS conduct an audit before the rates go into effect. ORS requested that the Commission provide clarification regarding the parameters of the audit.

Legal counsel further advised the Commission that the remaining issues to be resolved mainly involved accounting issues concerning expenses and depreciation.

FINDINGS OF FACT AND EVIDENCE SUPPORTING FINDINGS OF FACT

After thorough consideration of the entire record in the Midlands hearing, including the testimony and all exhibits, and the applicable law, the Commission makes the following findings of fact and conclusions of law with respect to Midlands:

1. Midlands is a closely held privately owned corporation furnishing sewer collection and sewer treatment service to 2,937 residential and commercial customers in Richland, Lexington, Fairfield, and Orangeburg Counties and is subject to the jurisdiction of the Commission pursuant to S. C. Code Ann Section 58-5-10 et seq.

The evidence supporting this finding is contained in the application filed by Midlands, in the testimony of Midlands' witnesses, Mr. Keith Parnell and Mr. Ken Parnell, and in prior Commission Orders in the docket files of the Commission, of which the Commission takes judicial notice. By filing its application, Midlands admits that it is a public utility within the meaning of S.C. Code Ann Section 58-5-10 and submits itself to the jurisdiction of the Commission.

2. The appropriate test year period for purposes of this proceeding is the twelve month period ending June 30, 2004.

Midlands chose to file its application on the twelve months ending June 30, 2004. Accordingly, Midlands picked the test year ending June 30, 2004. Based on Midlands' proposed test year, the ORS utilized the same test year period for its accounting and pro forma adjustments. A fundamental principle of the rate making process is the establishment of a historical test year with the basis for calculating a utility's operating margin and, consequently, the validity of the utility's requested rate increase. The test

year is established to provide the basis for making the most accurate forecast of the utility's rate base, reserves, and expenses in the near future when the prescribed rates are in effect. *Porter v. South Carolina Public Service Commission*, 328 S.C. 222, 493 S.E.2d 92 (1997), citing *Hamm v. S. C. Pub. Serv. Comm'n*, 309 S.C. 282, 422 S.E. 2d 110 (1992). While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year changes in expenses, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. Where an unusual situation exists which shows that the test year figures are atypical, the Commission should adjust the test year data. See *Southern Bell v. The Public Service Commission*, 270 S.C. 590, 244 S.E. 2d 278 (1978); see also, *Parker v. South Carolina Public Service Commission*, 280 S.C. 310, 313 S.E.2d 290 (1984), citing *City of Pittsburgh v. Pennsylvania Public Utility Commission*, 1887 P.A. Super. 341, 144 A.2d 648 (1958); *Southern Bell v. The Public Service Commission*, 270 S.C. 590, 244 S.E.2d 278 (1978). Based on the information available to the Commission, the Commission is of the opinion, and, therefore, concludes that the test year ending June 30, 2004 is appropriate for the purposes of this rate request.

3. The Commission will use the operating margin as a guide in determining the lawfulness of Midlands' proposed rates and for the fixing of just and reasonable rates.

In its application, Midlands does not specify or propose a particular rate setting methodology. "The Public Service Commission has wide latitude to determine an appropriate rate-setting methodology." *Heater of Seabrook v. Public Service*

Commission of South Carolina, 324 S.C. 56,64, 478 S.E.2d 826,830 (1996). ORS, in support of its position and recommendations in this case, presented in its exhibits and testimonies information regarding the operating margins for per books test year, test year as adjusted, Phase-I of the proposed increase, adjustments for After Construction Operations, and computation of the After Construction Operating results after Phase-II. Hearing Exhibit 14, Audit Exhibit A and late filed Exhibit 15 - Corrected Audit Exhibit A-1. ORS also presented various alternative operating margins and associated revenue requirements for these operating margins. Hearing Exhibit 13, Exhibit DMH-9. Midlands' neither supplied any operating margin information in its Application, nor supplied sufficient information on which rates could be set using rate of return on rate base methodology. Because the only information available relates to operating margin methodology, the Commission finds that the operating margin is the appropriate rate-setting methodology to use in this case.

4. Midlands is seeking an increase in rates in two phases. By its Application, Midlands is seeking an increase in its rates and charges, net of uncollectibles, for sewer service pursuant to a two-phase approach which Midlands asserts results in additional monthly revenues to the monthly revenue generated during the test year ending June 30, 2004, of \$26,353 during Phase-I and \$29,282 during Phase-II. As will be demonstrated infra, we believe that a Phase-I increase in revenues of \$389,057, and an additional increase in revenues of \$36,564 in Phase-II is appropriate.

The evidence for this finding concerning the amount of the requested rate increase is contained in the Application (as amended) by Midlands. Midlands' Application (as

amended), Exhibit 2, Pp. 1 through 7. The testimony and exhibits of ORS witnesses Dawn Hipp and Roy Barnette, as adjusted for adjustments approved herein, reveal that the level of total operating revenues under Phase-I of the rates are \$1,342,506, which reflects adjustments as approved herein and a net authorized increase in operating revenues of \$389,057. With respect to Phase-II, the testimony and exhibits of ORS witnesses Dawn Hipp and Roy Barnette, as adjusted for adjustments approved herein, show the level of total operating revenues after implementation of Phase-II of the rates are \$1,379,071, which reflects adjustments approved herein and a net authorized increase in operating revenues of \$36,564.

5. The appropriate operating revenues of Midlands during the test year under present rates and after accounting and pro forma adjustments are \$953,449.

Midlands' Application shows per book test year total operating revenues of \$956,194. Midlands' Application (as amended), Exhibit 2, P. 1 of 7. ORS verified the per book balances to the books and records of Midlands. The book figures reflect that Operating Revenues for Midlands totaled \$956,500 including interest income of \$306. ORS proposes to adjust revenues to reflect test year customer billings in the amount of (\$335,652) and to remove interest earned on the CD in the amount of (\$306) from other income - interest. ORS also proposed to reclassify Tap Fees to Contributions in Aid of Construction.

The Commission adopts the number of single family equivalents ("SFEs") and revenue as calculated by ORS. See Revised Exhibit DMH-6. However, the Commission finds that, based on the testimony of Company witness Keith Parnell and ORS witness

Dawn Hipp, the only pass-through treatment expenses are for those customers having treatment provided by the Town of Winnsboro. According to ORS calculations, this amount was \$8,826 for the test year. Therefore, the Commission finds that the test year calculated revenues provided by ORS of \$932,972 should only be reduced by \$8,826, to reflect pass-through treatment expenses for those customers having treatment provided by the Town of Winnsboro. Including this adjustment produces Service Revenue as adjusted of \$924,146. After including Other Revenue of \$29,303, Total Operating Revenue as adjusted is \$953,449. Further, tap fees are not revenue to the utility because tap fees are paid by the customer and are properly recorded as a rate base item in Contributions in Aid of Construction. We find the other revenue adjustments proposed by ORS to be reasonable and adopt the ORS' other revenue adjustments. Therefore, we find the appropriate total operating revenues for the test year after accounting and pro forma adjustments to be \$953,449.

6. The appropriate operating expenses for Midlands for the test year under present rates and after accounting and pro forma adjustments are \$1,001,573.

The parties offered certain adjustments affecting operating expenses for the test year. Midlands' witnesses, Mr. Keith Parnell and Mr. Ken Parnell, and ORS witnesses Mr. Willie Morgan, Ms. Dawn Hipp and Mr. Roy Barnette offered testimony and exhibits detailing adjustments proposed by the parties. See Hearing Exhibits 1, 2, 3, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, and Midlands' Application, as amended. This section addresses the adjustments to expenses.

(A) Officers' Salaries

(1) Position of Midlands: Midlands proposes to increase officers' salaries in the amount of \$19,808. Mr. Keith Parnell, in his Rebuttal Testimony states that the \$19,808 is intended as compensation for Ken Parnell who has put in substantial hours attending meetings, helping with loan matters, planning and providing engineering expertise. Mr. Keith Parnell contends that Mr. Ken Parnell has saved Midlands customers significant dollars through his participation and contribution to Midlands and that he should not be expected to donate his time. Prefiled Rebuttal Testimony of Keith G. Parnell, P.5, ll. 2-7, Hearing Exhibit 2.

(2) Position of ORS: ORS determined that no salary increases were given during the test year, and, therefore, no adjustment was necessary. Prefiled Direct Testimony of Barnette, P. 6 ll. 15; Hearing Exhibit 14, Corrected Audit Exhibit A-1.

(3) Decision of the Commission: The Commission finds that an Officer's Salary for Mr. Ken Parnell should be approved. The record reflects that Mr. Ken Parnell has performed numerous engineering duties for the Company and has been heavily involved in obtaining financing and provided planning and engineering expertise related to new treatment plants. See Rebuttal Testimony of Mr. Keith Parnell.

(B) Repairs - Non-Plant Maintenance

(1) Position of Midlands: Midlands proposes no adjustment.

(2) Position of ORS: ORS proposes to reduce repairs and non-plant maintenance expenses for personal travel and miscellaneous expenses in the amount of \$1,085 of Mr. Charles Parnell paid for by Midlands.

(3) Decision of Commission: Mr. Charles Parnell is the former owner of Midlands but is no longer employed by Midlands. Payment of personal travel expenses or other expenses of Mr. Charles Parnell is not payment of utility expenses incurred in providing utility services. Because ORS did not find justification for this adjustment and these repairs and expenses are unrelated to the utility operations of Midlands, these amounts are not allowed. Therefore, ORS' adjustment is adopted.

(C) Expenses for Repairs

(1) Position of Midlands: Mr. Keith Parnell contends that the \$16,692 should remain in the expense category since Midlands' operating history reflects at least that amount or more annually in breakage to plant and equipment. Rebuttal Testimony of Keith G. Parnell, P. 5, ll. 8-13, Hearing Exhibit No. 2. Midlands proposed to increase the expense by \$228.

(2) Position of ORS: ORS proposes to reduce operational and management expenses - plant maintenance and reclassify several items to plant. ORS determined these expenses were in fact capital expenditures because the items had a service life of more than one year. These items total \$16,692 and include such items as pipe, computers, motors, drives, and casing. See, Hearing Exhibit 14, Exhibit A-2. ORS determined that Midlands' proposal to increase this expense by \$228 was an estimate.

(3) Decision of Commission: The Commission did not find Midlands' adjustment to be a known and measurable cost since it is an estimate and attributed to rounding. The Commission adopts ORS capitalization of these items to plant and equipment. As the

items reclassified by ORS have a service life of more than one year, these items are properly capitalized rather than expensed.

(D) Chemical Expense

(1) Position of Midlands: Midlands proposed to reduce chemical expense by \$639.

(2) Position of ORS: ORS proposes no adjustment to operation and maintenance expense for chemicals. ORS determined that Midlands' proposal to decrease chemical expense by \$639 is due to rounding.

(3) Position of Commission: Because no justification was provided by Midlands as to the necessity of this adjustment, we find that no adjustment is appropriate and adopt ORS' position on this issue.

(E) Auto/Truck/Other Expense

(1) Position of Midlands: Midlands did not adjust expenses for this item.

(2) Position of ORS: ORS proposes to reduce operation and maintenance expense in the amount of \$825 for personal charges to Mr. Charles Parnell's American Express card which were paid by Midlands.

(3) Position of Commission: We find no justification for personal charges of Mr. Charles Parnell being paid by Midlands. These charges have not been shown to be necessary utility expenses for the provision of utility services; therefore, we find ORS' adjustment to be appropriate, and we adopt ORS' adjustment. Operation and maintenance expense will be reduced in the amount of \$825 for personal charges to Mr. Charles Parnell's American Express card which were paid by Midlands.

(F) Vehicle Expense

(1) Position of Midlands: Midlands proposed an adjustment of \$1,695 for increased insurance premiums.

(2) Position of ORS: ORS proposes to increase operation and maintenance expense - vehicle expense to record Midlands' proportional share of insurance premiums paid by Bush River Utilities, Inc. ("BRUI"). BRUI paid insurance premiums related to vehicles in the amount of \$3,926 during its test year ending December 31, 2003. Of that amount \$808 was determined to be for insurance coverage on personal vehicles and, therefore, not allowable. The balance of the insurance premiums of \$3,118 was allocated to Midlands and BRUI based on single family equivalents. Single family equivalents were 2,937 (69.09%) for Midlands and 1,314 (30.91%) for BRUI. Therefore, Midlands would be charged 69.09% of \$3,118, or \$2,154 and BRUI charged 30.91% of \$3,118, or \$964. Midlands proposed an adjustment of \$1,695, which ORS determined to be an estimate. Prefiled Testimony of Barnette, P. 7, ll.8-17, Hearing Exhibit No. 14, Corrected Audit Exhibit A-1.

(3) Decision of Commission: Midlands' proposed adjustment is not known and measurable. We find that ORS adjustments are appropriate as ORS disallowed expenses not related to utility operations and provided a reasonable calculation for allocating an expense shared by BRUI and Midlands. The Commission approves an increase to vehicle expenses of \$2,154 as proposed by ORS.

(G) Truck Expense

(1) Position of Midlands: Midlands proposed no adjustment.

(2) Position of ORS: ORS proposed to adjust operation and maintenance expense - vehicle expense to allocate truck expenses to assign one-third (1/3) of the expense to Midlands. Midlands stated it used the Ford F-250 owned by Developmental Services, Inc. ("DSI") one-third (1/3) of the time. Total truck expenses as reflected on the DSI books amount to \$1,109 which is comprised of \$858 for vehicle insurance and \$251 for vehicle repairs. One third (1/3) of \$1,109 is \$370; therefore, to allow one-third (1/3) of the truck expense, ORS' adjustment is \$370.

(3) Decision of Commission: Midlands did not contest this adjustment. We find that the adjustments are reasonable and adopt them. Thus, the amount of one-third (1/3) of the truck expense, or \$370, shall be allocated to Midlands.

(H) Taxes Other Than Income

(1) Position of Midlands: Midlands proposed no adjustment.

(2) Position of ORS: ORS proposes to adjust Taxes Other Than Income for one-third (1/3) of the total vehicle taxes paid by DSI on a Ford F-250 truck. Midlands states that it used the truck one-third (1/3) of the time. The total taxes as booked by DSI were \$328, and, therefore, an adjustment of \$109 was required to allocate one-third (1/3) of that expense to Midlands.

(3) Decision of Commission: We find that the adjustment of ORS is appropriate, and we adopt this adjustment.

(I) Utilities Expense

(1) Position of Midlands: Midlands proposed a reduction to utilities expense in the amount of \$963.

(2) Position of ORS: ORS does not propose an adjustment to the utilities expense account, and ORS determined Midlands proposed reduction of \$963 was an estimate.

(3) Decision of Commission: Midlands' proposed adjustment is not known and measurable. Because the adjustment cannot be verified, Midlands' proposed reduction to utilities expense is not allowed.

(J) Insurance Expense

(1) Position of Midlands: Midlands did not propose an adjustment.

(2) Position of ORS: ORS proposes to allocate to Midlands a portion of insurance costs paid by BRUI for general liability and umbrella coverage on commercial property. BRUI paid premiums totaling \$1,180. ORS allocated this balance among the three (3) affiliated companies based on the percentage of single family equivalents. Single family equivalents (SFEs) were 2,937 (54.09%) for Midlands; 1,314 (24.20%) for BRUI; and 1,179 (21.71%) for DSI. ORS allocated \$638 [the product of the total premiums of \$1,180 multiplied by 54.09% which reflects Midlands' portion of total SFEs served by the three companies] to Midlands. Prefiled Testimony of Barnette, P. 8, ll. 10-16. Hearing Exhibit 14, Audit Exhibit A-2.

(3) Decision of Commission: Midlands did not contest the adjustment of ORS. The Commission finds ORS' proposed adjustment is reasonable, and we adopt this adjustment. Insurance expense shall be allocated to Midlands in the amount of \$638.

(K) Vehicle Insurance Expense

(1) Position of Midlands: Midlands did not propose an adjustment.

(2) Position of ORS: The Company paid a total of \$10,109 for insurance coverage on vehicles. The ORS proposed to reduce vehicle insurance expenses by \$2,079 for premiums that were related to coverage of personal vehicles that were carried on the Midlands' insurance policy. The ORS also proposed to allocate the remaining amount, or \$8,030, between MUI and BRUI based on single family equivalents. The ORS determined the amount to be allocated to BRUI to be \$2,482 or 30.91% of the \$8,030. The total proposed ORS adjustment consisted of a reduction of \$2,079 for personal insurance premiums and a reduction of \$2,482 for premiums allocated to BRUI for a total reduction to expenses of \$4,561.

(3) Decision of Commission: The Commission finds that vehicle insurance premiums that are related to personal vehicles should not be included in the expenses of the Company. The Commission also finds that the ORS has properly allocated the remaining vehicle insurance premiums between the Company and BRUI. The Commission adopts the proposed adjustment of the ORS to reduce vehicle insurance premiums expense by \$4,561.

(L) Insurance Premiums

(1) Position of Midlands: Midlands proposes to increase insurance expenses by \$8,705.

(2) Position of ORS: ORS determined Midlands' proposal to be an estimate. ORS proposes to reduce O&M expenses for insurance costs for General Liability and Umbrella premiums paid by Midlands for the benefit of BRUI and DSI. During the test year, Midlands made various payments to Auto Owners Insurance Companies for these

coverages totaling \$3,646. ORS proposes to allocate these premiums to the three affiliated companies based upon single family equivalents, i.e., Midlands 2,937 (54.09%); BRUI 1,314 (24.20%); and DSI 1,179 (21.71%). Therefore, ORS proposes to allocate to BRUI \$3,646 multiplied by 24.20%, or \$882, and to DSI \$3,646 multiplied by 21.71%, or \$792, for a total allocation adjustment of (\$1,674). ORS Witness Barnette, Direct Testimony, P. 9, ll. 6-14 and Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: The Commission finds ORS' adjustments and manner in arriving at these adjustments to be reasonable and verifiable. The ratepayers of Midlands should not be charged for expenses incurred by its sister companies. The Commission allows the ORS recommended adjustments to reduce Midlands' general liability and umbrella insurance by \$1,674.

(M) Treatment Costs

(1) Position of Midlands: Midlands proposes to increase O&M expenses for treatment in the amount of \$110,979.

(2) Position of ORS: ORS proposes to remove treatment costs of \$265,021 as this is a pass through expense for collection only customers. The collection only customers will be charged back for their proportionate share of treatment cost when the bill is received by Midlands from the treatment provider. Therefore, in establishing a collection only rate, ORS proposes that these treatment costs be removed. ORS Witness Barnette, Direct Testimony, P. 9, ll. 15-21, and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Position of Commission: The Commission approves the increase to outside Treatment Expenses of \$110,979 as proposed by the Company. This amount was uncontested by ORS since all outside treatment costs were eliminated. However, these treatment costs are not a pass-through expense for collection only customers as alleged by ORS. Consistent with our findings contained herein concerning revenue adjustments, we find that the proposed treatment costs should be decreased by \$8,826 to eliminate pass-through treatment costs for those customers having treatment provided by the Town of Winnsboro. We find that all other customers receiving outside treatment are being billed the approved collection and treatment rate as if Midlands was providing treatment. Therefore, Treatment Expense as adjusted is \$367,174.

(N) **Service Contracts**

(1) Position of Midlands: Midlands proposes to increase O&M expenses in the amount of \$27,120 as a payable due to DSI. Midlands' rationale is that Midlands operates and maintains two pieces of equipment that are owned by DSI. The two pieces of equipment are a backhoe and a generator that are necessary for Midlands' operation of the sewer system. Midlands operates DSI's 420D backhoe 65% of the time and operates DSI's XQ125 generator 100% of the time. Midlands' position is that the weekly, monthly or annual rental from any commercial company leasing this equipment would more than exceed the agreed upon value established between Midlands and DSI. Mr. Parnell provided a quote for a monthly rental of DSI's backhoe of \$1,500 a month and a monthly rental of DSI's generator of \$2,625 per month. Midlands' position is also that DSI purchased the equipment which benefited Midlands' customers. Midlands also

presented a rental agreement dated February 23, 2005 concerning Midlands' rental of the equipment. Midlands Witness Keith G. Parnell, Hearing Exhibit 2, Rebuttal Testimony, Pp. 5 – 6; Hearing Exhibit 3.

(2) Position of ORS: ORS found no actual payments during the test year and no Account Payable on the books and records of Midlands and disallowed the proposed adjustment. During the DSI rate case, DSI proposed to increase its revenues to account for rental "payments" by Midlands for use of this equipment. DSI proposed to charge Midlands \$27,120 for the use of DSI's equipment. No contract was issued, and ORS determined the adjustment to be unallowable. The Commission in Docket No. 2004-212-S, Order No. 2005-42 dated February 2, 2005, agreed with ORS in its determination. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 10, ll. 1-7 and Surrebuttal Testimony, P. 3, ll. 7-14.

(3) Decision of Commission: Midlands witness Keith G. Parnell testified at the hearing that Midlands did not pay DSI the "contract" payment \$27,120 for the use of the equipment in the test year or after the test year and that no documentation was available concerning the rental during the test year. Cross examination of Witness Keith G. Parnell, Hearing Transcript, Pp. 65-66. Additionally, the contract offered by Midlands was dated on February 23, 2005, which was the day before the hearing in this case. This contract was not available to the ORS during its audit and, in fact, was not executed until approximately eight months after the end of the test year. It appears that the contract was prepared solely to obtain recovery of alleged expenses which have not been paid or even booked as an Account Payable. Because Midlands did not pay the expense to DSI, did

not book the expense as an Account Payable, and did not have a contract for the expense until the eve of this hearing, we find no realistic justification of an actual expense. Furthermore, we find that the backhoe and generator in question was properly allocated by ORS among the three (3) utilities based on usage and that the Company is recovering its investment in such equipment through Depreciation Expense over its useful life. Therefore, the Commission agrees with the position of ORS and disallows Midlands' proposed adjustment.

(O) Salaries Other

(1) Position of Midlands: Midlands proposes an adjustment of \$3,450 for increase in salaries.

(2) Position of ORS: ORS determined that one employee received a salary increase during the latter part of the test year. ORS proposes to adjust for the increase. Total annualized wages were calculated to be \$216,298 with total booked wages of \$211,742 resulting in an adjustment of \$4,556. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P.10, ll. 8-12 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: The adjustment of ORS is verified and reflects a known and measurable change. The Commission adopts the adjustment of ORS.

(P) Professional Fees for Legal and Consulting

(1) Position of Midlands: On Midlands' books, three accounts, Attorney Fees (\$102,877), Legal Fees (\$37,226), and Consulting Fees (\$23,540) total \$163,643 and represent professional fees.

(2) Position of ORS: ORS proposes to adjust these amounts. Although some of these amounts were paid during the test year, a portion of these fees were for services provided to Midlands in previous years or were determined to be non-allowable for rate making purposes. Most of these invoices were billed by Austin, Lewis and Rogers, P.A. and pertained to the 208 Plan Amendments or for services outside the test year dealing with litigation involving Midlands vs. City of Cayce. Following ORS' review of these accounts, it was determined that \$47,464 was unallowable as lobbying expenses or was paid for services outside the test year. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 10, ll. 13-22 and Hearing Exhibit 15, Corrected Audit Exhibit A-1. ORS Witness Barnette testified that the \$47,464 that was disallowed by ORS was comprised of \$19,415 for lobbying, which ORS does not consider to be an allowable expense for ratemaking, \$666 related to the filing of the loan documents, and \$27,383 in payments for services received outside the test year. ORS Witness Barnette, Hearing Exhibit 14, Surrebuttal Testimony, P. 3, ll. 17 -23.

(3) Decision of Commission: The Commission finds ORS' adjustments to be of sound regulatory policy and also to be known and measurable. We find that lobbying expenses are not an item upon which rates should be based. Further, the costs associated with the filing of the loan documents are expenses of the loan and should be treated as such. We therefore accept ORS' adjustment and find that \$47,464 of the legal, consulting, and attorneys fees should be disallowed.

(Q) Other Operating Expenses

(1) Position of Midlands: Midlands proposed to increase Other Operating Expenses by \$1,612.

(2) Position of ORS: ORS determined that \$272 travel charges for personal travel expenses unrelated to company business on Mr. Charles Parnell's American Express account were paid by Midlands. ORS reduced G & A by \$272. ORS determined that Midlands' proposed increase of \$1,612 was an estimate. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P, 11, ll. 1-5 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: Midlands' adjustment is not known and measurable. Further, the personal travel expenses unrelated to utility operations are not recoverable because those expenses were not incurred in the provision of utility services. Therefore, the Commission accepts ORS' adjustment.

(R) Telephone and Office Expense

(1) Position of Midlands: Midlands proposes to increase this account by \$449.

(2) Position of ORS: ORS proposes to reduce telephone and office expense in the amount of \$181. ORS proposes to remove a \$50 cash contribution made to Dunn's Chapel Church and \$131 of telephone bills paid by Midlands for BRUI. ORS determined Midlands' proposed increase to be due to rounding. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 11, ll. 6-9 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: ORS Witness Barnette testified that this adjustment appears to be due to rounding. Because the adjustment cannot be verified, Midlands' adjustment cannot be accepted. The Commission approves the adjustment of ORS to reduce telephone and office expense in the amount of \$181 to remove a charitable contribution and an expense related to another utility.

(S) DHEC Fines

(1) Position of Midlands: Midlands proposes to increase DHEC fines by \$9,549.

(2) Position of ORS: ORS proposes to eliminate DHEC fines of \$30,451, as they are not considered a normal business expense. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 11, ll. 10-12, and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: The Commission adopts the adjustment of ORS. Customers should not be required to absorb the cost of DHEC fines as these fines are not a normal business expense. The utility is required to operate in compliance with the law. Rate payers should not pay for violations of the utility in rates.

(T) Administrative Expenses

(1) Position of Midlands: Midlands did not have an adjustment for administrative expenses.

(2) Position of ORS: ORS proposes to reduce Administrative expenses by \$3,254. ORS verified the booked expenses related to Administrative expenses. During the performance of the audit of BRUI, ORS determined the Administrative expenses of both BRUI and Midlands are paid by Midlands. ORS compiled those expenses that make

up this category of expense from the books and records of Midlands. Since Midlands has a fiscal year ending June 30th, ORS took a two-year average of all expenses in the category in an effort to estimate the appropriate allocation of Administrative expenses on the books of BRUI. ORS' calculation indicated that the expenses to be allocated totaled \$88,173. The average expenses were then allocated to each company based upon single family equivalents, with Midlands bearing 69.09% of the expense and BRUI bearing 30.91% of the expenses. ORS recommends that an additional \$3,254 in Administrative expense be allocated to BRUI, with a corresponding reduction to the books of Midlands of (\$3,254). ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 11, ll. 13-22 and P. 12, ll. 1-2 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of the Commission: The Commission finds ORS' adjustments and the manner in arriving at these adjustments to be reasonable and verifiable. The Commission will allow these expenses to be allocated to Midlands and BRUI. The Commission also finds ORS' allocation based on single family equivalents reasonable and appropriate for regulatory purposes and approves ORS' recommended adjustments to reduce Midlands' Administrative expenses by \$3,254.

(U) Loan Costs

(1) Position of Midlands: Midlands proposes to amortize loan costs of \$81,591. Midlands proposes to amortize Midlands' proportionate share of these loan costs at the rate of \$1,500 per year over a twenty (20) year period.

(2) Position of ORS: ORS disallows this adjustment and proposes that all loan costs be capitalized and no amortization be recognized. By capitalizing these costs,

Midlands will recover the loan costs through depreciation expense over the useful life of the asset to be constructed with the loan proceeds. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 12, ll. 3-8 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: The Commission concurs with the adjustment of ORS, and all loan costs will be capitalized by Midlands.

(V) Amortization of Two and one-half months of Loan Cost

(1) Position of Midlands: Midlands proposes to amortize two and one-half (2 ½) months of total loan costs, or \$680, based on a useful life of twenty five years.

(2) Position of ORS: ORS proposes to capitalize loan costs and depreciate the costs over the useful life of the asset. Since the asset has yet to be placed in service, ORS disallows this adjustment. This amount was included in Other Operating Expenses on Midlands' books. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 12, ll. 9-12 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: The Commission concurs with the recommendation of ORS. Since the asset has yet to be placed in service, the Commission disallows Midlands' proposal to amortize two and one-half (2 ½) months of total loan costs.

(W) Rate Case Expenses

(1) Position of Midlands: Midlands proposes to adjust G&A expense for rate case expenses associated with its filing. In its application, originally Midlands proposed

\$20,000 in rate case expenses. Midlands filed a late filed exhibit adjusting attorneys' fees and costs for the rate case. See Hearing Exhibit 8.

(2) Position of ORS: ORS proposed to amortize total rate case expenses of \$27,736 over a five (5) year period for a total adjustment of \$5,547. ORS' adjustment is comprised of \$1,000 for expenses for accounting services incurred after the test year, \$25,650 for incurred legal expenses and newspaper advertisements in *The Times and Democrat* of \$104 and *The State* of \$982, for total rate case expenses of \$27,736. ORS examined the time between rate cases as one measure for an amortization period. Midlands' previous rate case proceedings were in 1991 and 1997 resulting in an average of approximately seven (7) years between rate cases. ORS determined a seven (7) year amortization period is too long; therefore, ORS proposes to use a more reasonable amortization period of five (5) years for recovery of rate case expenses. ORS Witness Barnette, Hearing Exhibit 14, Direct Testimony, P. 12, ll. 13-22 and P. 13, ll. 1-2 and Hearing Exhibit 15, Corrected Audit Exhibit A-1.

(3) Decision of Commission: The Commission concludes that a three-year amortization period is a reasonable period for Midlands to recover these expenses without causing undue hardship on ratepayers. While no one can accurately predict when the utility will present another case for a rate increase, the Commission has approved both Phase-I and Phase-II of the requested rates. The Commission will therefore allow updated rate case expenses of \$39,590 to be recovered over a three year period for an adjustment of \$13,197. In addition, because we are approving both phases of Midlands' requested increase and the second phase will not be implemented until construction of the

upgrades to the facilities is completed, we find that an amortization period of three years is reasonable. Additionally, due to our findings included herein regarding a Phase II increase, the Company could be involved in further regulatory proceedings before implementation of Phase II rates.

(X) Payroll Taxes

(1) Position of Midlands: Midlands does not propose an adjustment.

(2) Position of ORS: ORS proposes to adjust Taxes Other Than Income – Payroll taxes to reflect the change in taxes resulting from the annualized wages adjustment. Payroll taxes based upon annualized wages totaled \$16,547 (\$216,297 times 7.65%). Payroll taxes booked for the test year were \$14,555. Therefore, the payroll tax adjustment is (\$16,547-\$14,555) or \$1,992. Direct Testimony of Barnette – P. 13, ll. 11-15.

(3) Decision of Commission: The Commission finds ORS' adjustments of \$1,992 reasonable and adopts this adjustment.

(Y) License and Fees

(1) Position of Midlands: Midlands does not propose an adjustment for license and fees.

(2) Position of ORS: ORS proposes to adjust Taxes Other Than Income – License and Fees for two items totaling \$575 determined to be non-allowable, i.e. SC Jobs – Economic Development Authority – application fee of \$500 to apply for JEDA Bond and Mr. Charles Parnell's annual membership fee to American Express of \$75.

(3) Decision of Commission: The Commission finds no testimony or evidence to show that these expenses are necessary in the provision of utility services. The application

fee for JEDA Bond (\$500) and Mr. Charles Parnell's annual American Express membership fee are, therefore, disallowed.

(Z) Interest Expense for Service Charges

(1) Position of Midlands: Midlands has listed the service charges from Ben Satcher (\$43) and P&S Construction (\$8) as Interest Expense.

(2) Position of ORS: ORS proposes to credit Interest Expense for service charges paid to Ben Satcher Motors (\$43) and P&S Construction (\$8), a total of (\$51), and charge them to O&M Expenses – Truck Expense and Repairs.

(3) Decision of Commission: The Commission finds that the service charges in the amount of \$51 should be reclassified from Interest Expense to O & M Expense. The identified expenses are not properly included in Interest Expense. The Commission finds ORS' adjustments and manner in arriving at these adjustments to be known and measurable.

(AA) Reclassification of Truck Expenses and Repairs

(1) Position of Midlands: Midlands did not propose an adjustment.

(2) Position of ORS: ORS proposes to charge O&M Expense – Truck Expense and Repairs for service charges paid to Ben Satcher Motors (\$43) and P&S Construction (\$8), a total of \$51 and credit Interest Expense. This adjustment is a result of reclassification of expenses removed from Interest Expense.

(3) Decision of Commission: The Commission adopts the ORS position to reclassify service charges from Ben Satcher (\$43) and P&S Construction (\$8) from interest expense to O&M expense and repairs.

(BB) BB&T Interest Expense

(1) Position of Midlands: Midlands proposes to allow \$885 associated with loan costs from the BB&T Loan as interest expense.

(2) Position of ORS: ORS proposes to remove, as unallowable, interest expense of (\$885) paid to BB&T associated with Loan Costs, since ORS determined that all loan costs should be capitalized and depreciated over the useful life of the asset.

(3) Decision of Commission: The Commission finds ORS' proposal to be in accordance with regulatory accounting principles and recognizes these costs should be treated as loan costs and not expensed. The Commission disallows Midlands' proposal to classify the \$885 associated with loan costs as an interest expense.

(CC) Lexington County Property Taxes

(1) Position of Midlands: Midlands proposes no adjustment to Lexington County Property Taxes.

(2) Position of ORS: ORS proposes to allocate to BRUI and DSI their proportionate share of Lexington County property taxes. During the test year, Midlands paid a total of \$5,190 in property taxes to Lexington County, consisting of property taxes of \$2,354 on the corporate office building and \$2,836 on four (4) trucks and two (2) trailers. ORS proposes to allocate the taxes on the corporate office building based on single family equivalents with 24.20% or \$570 allocated to BRUI and 21.71% or \$511 allocated to DSI. The remainder of the property taxes on the corporate office or 54.09% equaling \$1,273 will remain as a Midlands expense. Midlands proposes to allocate the property taxes on the four (4) trucks and two (2) trailers of \$2,836 based on various usage factors provided by

Midlands with the majority of the expense remaining with Midlands. Based on the factors provided by the company, \$211 was allocated to BRUI and \$211 to DSI. The remainder of the property taxes on the trucks and trailers, or \$2,414 will remain as a MUI expense. Therefore, the total allocation to BRUI is \$781 and DSI is \$722 for a total reduction to Midlands' expenses of \$1,503.

(3) Decision of Commission: We find ORS' adjustments to be appropriate and adopt them as computed. ORS' proposed allocation requires each of the three utilities to bear its proportionate share. Accordingly, the property taxes on Midlands' books shall be reduced by \$1,503 to reflect BRUI's and DSI's share of the Lexington County property taxes.

(DD) Interest Expense on Customer Deposits

(1) Position of Midlands: Midlands proposes an adjustment to interest expense of \$32,756.

(2) Position of ORS: ORS proposes to adjust Interest Expense to reflect the correct expense for interest on customer deposits. In Docket No.1996-013-A, Order No. 2003-593 dated October 3, 2003, the Commission approved a reduction in rates on customer deposits from 8%, which was approved by Order No. 93-12, to 3.5%. ORS calculated the adjustment based on Customer Deposits on the books at June 30, 2004 of \$58,600 multiplied by 3.5% which equals \$2,051. Midlands previously had interest recorded on the books of \$1,813; therefore, the interest adjustment is \$2,051 less \$1,813 or \$238. It should be noted, however, that since this calculation is made on a going forward basis, interest will still be due and payable at 8% to those customers who had deposits with MUI prior to

December 31, 2003. According to the books and records of Midlands, the Customer Deposits account had a balance of \$56,586 as of December 31, 2003.

(3) Decision of Commission: The Commission approves the adjustment of ORS to adjust interest expense on Customer Deposits in the amount of \$238 to reflect the proper expense as of the end of the test year. The Commission finds ORS' adjustments to be known and measurable.

(EE) Plant Depreciation expense

(1) Position of Midlands: Midlands proposes to decrease depreciation in the amount of \$293 which ORS determined to be an estimate.

(2) Position of ORS: ORS proposes to increase depreciation expense for plant in service by \$7,025. This adjustment results from several factors, and the calculation of the total is illustrated in Audit Exhibit A-2. See Hearing Exhibit 14. First, ORS proposes to adjust depreciation expenses using service life periods recommended by the Water/Wastewater Department. The Water/Wasterwater Department proposes basing depreciation rates based on Florida Public Service Commission Water and Wasterwater System Regulatory Law as recommended by NARUC. Accordingly, ORS recommends that the plant be depreciated over 32 years. Next, ORS proposes to allocate certain plant purchased by DSI that is also used by Midlands and BRUI. ORS also reduced the computed depreciation expense for the depreciation expense associated with tap fees. Tap fees are Contributions in Aid of Construction ("CIAC") and should be used to reduce rate base, rather than be included in revenue. ORS' adjustment removes depreciation expense on the plant paid for by CIAC.

(3) Decision of Commission: We find that ORS' adjustments are appropriate and adopt them as computed for existing plant.

(FF) Mary Parnell's Salary

(1) Position of Midlands: Midlands' position is that the salary paid to Mary Parnell in the amount of \$9,360 is a general and administrative expense.

(2) Position of ORS: ORS proposes to remove from G&A Expense – Salaries – Other, the salary paid to Mary Parnell during the test year of \$9,360. Mrs. Parnell has no official job position with MUL.

(3) Decision of Commission: Midlands' position does not reflect a known and measurable amount. Mrs. Parnell was not and is not an employee of Midlands. ORS' adjustment is appropriate, and the Commission adopts this adjustment. Mrs. Parnell's salary shall be removed from G&A expenses.

(GG) Payroll Taxes for Mary Parnell's Salary

(1) Position of Midlands: Midlands proposes to pay FICA and Medicare taxes on Mary Parnell's salary.

(2) Position of ORS: ORS proposes to reduce Taxes Other Than Income – for the payroll taxes associated with Mrs. Mary Parnell's salary of \$9,360. ORS calculated its adjustment: \$9,360 multiplied by 7.65% for FICA and Medicare taxes equals \$716.

(3) Decision of Commission: The Commission adopts the ORS proposed decrease to reduce taxes other than income by \$716. Midlands has provided no justification for Mary Parnell receiving a salary from Midlands.

(HH) Gross Receipts Taxes

(1) Position of Midlands: Midlands did not propose an adjustment to Gross Receipts Taxes based on as adjusted revenues.

(2) Position of ORS: ORS proposes to reflect the gross receipts taxes associated with the as adjusted revenue. The gross receipts factor includes cost for administration, the Public Service Commission and the Office of Regulatory Staff. The ORS adjustment is computed using the as adjusted revenue of \$612,692 multiplied by the gross receipts factor of 0.007733226 resulting in an amount of \$4,738 less the per book amount of \$6,564, for a net adjustment of (\$1,826).

(3) Decision of Commission: Since the Commission has adopted the revenue adjustments approved herein, it is appropriate to apply the most recent gross receipts factor for an amount of \$7,373 for Midlands' Gross Receipts Tax Expense, or an increase to the ORS adjustment of \$2,635.

(II) Uncollectibles associated with the As Adjusted Revenue

(1) Position of Midlands: Midlands does not propose an adjustment to uncollectibles for the as adjusted Revenue.

(2) Position of ORS: ORS proposes to adjust G&A expenses for a 1.5% allowance for uncollectibles associated with the as adjusted service revenues. The 1.5% allowance is an industry standard and is more than Midlands' actual test year uncollectible rate of 1.35%. ORS' adjustment used the As Adjusted Service Revenues of \$583,389 multiplied by the 1.5% allowance factor, for a total adjustment of \$8,751. See ORS Witness Barnette Testimony, P. 16, ll. 14-18.

(3) Decision of Commission: The Commission finds that the 1.5% uncollectible rate proposed by ORS and recognized as the industry standard is reasonable. The 1.5% factor requires an adjustment of \$13,862, based on our revenue findings included herein, or an increase to the ORS adjustment of \$5,111.

(JJ) Income Taxes

(1) Position of Midlands: Midlands does not propose to adjust for Income Taxes associated with the As Adjusted Revenue.

(2) Position of ORS: ORS proposes to adjust for income taxes associated with the As Adjusted Revenue. This increase is in the amount of \$2,061. See ORS Witness Barnette Testimony, P. 16, ll. 19-22.

(3) Decision of Commission: The Commission agrees with ORS that the Income Taxes associated with the As Adjusted Revenue should be adjusted. The utility operations are the source of the tax liability and coverage for the tax liability should be included in the Company's rates. The Commission finds that the appropriate adjustment to Income Taxes based on the adjustments approved herein should be \$(0) due to a net operating loss as adjusted.

7. The operating margin for the test year under present rates and after accounting and pro forma adjustments approved herein is (5.05%).

The calculation for the operating margin was based on using the test year adjusted operating revenues of \$953,449 as approved herein and test year as adjusted operating expenses of \$1,001,573 as approved herein. Adjusted test year operations result in a "Net Income(Loss) for Return" of (\$48,124). Using the adjusted Net Income(Loss) for Return

less Interest Expense divided by operating revenues, we calculate an operating margin of (5.05%).

Per book total operating expenses amounted to \$954,840 resulting in a per book net operating income after taxes of \$1,660. Customer growth of \$22 was computed on the per book net operating income resulting in per book total income for return of \$1,682. Using total income for return of \$1,682 and operating revenues of \$956,500, ORS computed a per book operating margin of 0.18%. The net effect of the accounting and pro forma adjustments approved herein decreased total income for return from \$1,682 to (\$48,124) and decreased the operating margin from 0.18% to (5.05%).

The following table indicates (1) Midlands' gross revenues for the test year after adjustments approved herein under the current rate schedule; (2) Midlands' operating expenses for the test year after accounting and pro forma adjustments and adjustments for known and measurable out-of test year occurrences approved herein; and (3) the operating margin under the presently approved schedule for the test year:

TABLE A

Before Increase As Adjusted

Operating Revenues	\$ 953,449
Operating Expenses	<u>1,001,573</u>
Net Operating Income/(Loss)	(\$48,124)
Add: Customer Growth	<u>0</u>
 TOTAL INCOME (LOSS) FOR RETURN	 <u>(\$48,124)</u>
 Operating Margin	 <u>(5.05%)</u>
(Interest Expense For Operating Margin)	<u>0</u>

8. Based on the need and requirement that Midlands upgrade certain of its wastewater treatment facilities pursuant to a Consent Order with DHEC, we find that Midlands has demonstrated a need for an increase in rates. Since adjusted test year operations reveal an operating margin of (5.05%), Midlands requires an increase in rates in order to upgrade its facilities to comply with the Consent Order and to meet permitting limits.

9. When applied to as adjusted test year operations, the rates requested and proposed by Midlands result in an operating margin of 15.79% for Phase-I and 13.84% for Phase-II. Information concerning the effect of the proposed rates when applied to as adjusted test year operations of Midlands is found in ORS exhibits introduced during the hearing and the Company's Application, as amended. The Commission finds that the rates proposed by Midlands for the Phase-I rate increase, would produce additional revenues of \$389,057 which results in an operating margin of 15.79%. We also calculate that the rates proposed by Midlands for the Phase-II rate increase would produce additional revenues of \$36,564 which results in an operating margin of 13.84% following implementation of Phase-II rates.

10. The Commission finds that the proposed increase as presented by Midlands is just and reasonable and will produce rates which are just and reasonable. Accordingly, the Commission approves the two-phase increase in rates as proposed by Midlands. The evidence and adjustments for the herein approved increase are discussed in this section.

ADJUSTMENTS ASSOCIATED WITH PHASE-I OF INCREASE:

(A) Service Revenue Adjustment for Proposed Increase

(1) Position of Midlands: Midlands proposes to adjust service revenues for the proposed increase on a net revenue basis of \$316,238.

(2) Position of ORS: ORS' proposed service revenue adjustment amounts to \$323,809 as provided by the Water/Wastewater Department. See ORS Witness Barnette Testimony P. 16, ll. 21-22.

(3) Decision of Commission: The Commission finds that the rates and charges proposed by the Company produce additional gross annual revenues of \$389,057 using the SFEs as computed by ORS and including the Company's current billing practices. The testimony of Midlands and the ORS reveals that the Company bills outside treatment customers the approved collection and treatment rate as if Midlands was providing the treatment. The record also reveals that the only pass-through rates being billed by the Company are for those customers having treatment provided by the Town of Winnsboro. Utilizing these billing practices under present and proposed rates, applied to SFEs as calculated by ORS, produces an increase in rates and charges of \$389,057.

(B) Gross Receipts Tax for the Proposed Increase

(1) Position of Midlands: Midlands does not propose an increase related to the Gross Receipts Tax for the Proposed Increase.

(2) Position of ORS: ORS proposes to reflect the gross receipts taxes associated with the proposed increase. The gross receipts factor includes cost for administration, the Public Service Commission and the Office of Regulatory Staff. The ORS adjustment is

computed using the Proposed Increase Revenue of \$323,809 multiplied by the gross receipts factor of \$0.007733226 resulting in an amount of \$2,504. See ORS Witness Barnette Testimony, P. 17, ll. 3-7; Audit Exhibit A-1, P. 4 of 5.

(3) Decision of Commission: The Commission believes an adjustment for gross receipts tax is reasonable and consistent with the previous adjustments. Since the Commission has adopted and approved the two-phase proposed increase in service revenue, it is appropriate to adjust the gross receipts tax in the amount of \$3,009.

(C) Uncollectibles associated with Proposed Increase (Phase I)

(1) Position of Midlands: Midlands does not propose an adjustment to uncollectibles for the As Adjusted Revenue.

(2) Position of ORS: ORS proposes to adjust expenses for a 1.5% allowance for uncollectibles associated with the proposed increase. The 1.5% allowance is an industry standard and is more than Midlands' actual test year uncollectible rate of 1.35%. ORS' adjustment used the proposed increase revenues of \$323,809 multiplied by the 1.5% allowance factor, for a total adjustment of \$4,857. See ORS Witness Barnette Testimony, P. 17, ll. 8-12; Audit Exhibit A-1, P. 4 of 5.

(3) Decision of Commission: The Commission finds the 1.5% uncollectible rate proposed by ORS and recognized as the industry standard to be reasonable. The 1.5% factor requires an adjustment of \$5,836 for the proposed increase (Phase1) based on our findings herein.

(D) Income Taxes associated with Proposed Increase to Revenues

(1) Position of Midlands: Midlands proposes an adjustment of \$28,452 to adjust income taxes associated with the proposed increase revenue.

(2) Position of ORS: ORS proposes an adjustment of \$119,394 to adjust for income taxes associated with the Proposed Increase to Revenue.

(3) Decision of Commission: The Commission agrees that the Income Taxes associated with the As Adjusted Revenue should be adjusted. The utility operations are the source of the tax liability and coverage for the tax liability should be included in the Company's rates. The Commission finds that the appropriate adjustment to Income Taxes based on the adjustments approved herein should be \$122,893.

ADJUSTMENTS ASSOCIATED WITH PHASE-II OF THE INCREASE:

(A) Service Revenues

(1) Position of Midlands: Midlands proposes to adjust the service revenue by a net revenue amount of \$35,150.

(2) Position of ORS: ORS proposes to adjust service revenues to reflect changes in revenues after construction. ORS' proposed an adjustment to service revenue in the amount of \$35,200. See ORS Witness Barnette Testimony, P. 17 ll. 16-18, Audit Exhibit A-1.

(3) Decision of Commission: The Commission agrees that the service revenues should be adjusted to reflect changes in revenues after construction. The Commission finds that the appropriate adjustment to service revenues after construction (Phase II) should be \$36,564 based on SFEs as calculated by ORS and the Company's current billing practices.

(B) Depreciation Expense

(1) Position of Midlands: Midlands proposes an adjustment of \$46,750 based on a 25 year service life period for the existing WWTFs.

(2) Position of ORS: ORS proposes to adjust depreciation expense for plant in service by \$34,062 using ORS recommended depreciation rates including plant upgrades proposed in Phase II. ORS reduced depreciation for expenses associated with Contributions in Aid of Construction. ORS also proposes to allocate certain plant in service to DSI and BRUI. See ORS Witness Barnette Testimony, P. 17-18, Audit Exhibit A-1, P. 5 of 5. The Water/Wastewater department proposes basing depreciation expense on depreciation rates found in the Florida Public Service Commission Water and Wastewater System Regulatory Law as recommended by NARUC. ORS recommends that the existing Midlands' wastewater treatment facilities ("WWTF") cost be capitalized and depreciated over a 32-year average service life and also that any new WWTFs cost be capitalized over a 32-year average service life period. Hearing Exhibit 9, Morgan Direct Testimony, P. 5, ll. 12-23, Audit Exhibit A-1, P. 5 of 5.

(3) Decision of Commission: Midlands, to support its request for a twenty-five year service life on treatment plant upgrades, offered testimony and three exhibits filed as a composite exhibit. Parnell Rebuttal Testimony and Hearing Exhibit 7, Exhibit 4. Of the composite exhibit, the first exhibit was an excerpt from a publication entitled The Design of Municipal Wastewater Treatment Plants, Volume I, pages 24, 69, 137, 141. However, the Commission finds this exhibit does not relate to the service life of the system upgrade

proposed by Midlands. Rather, it provides generalities that should be considered when constructing a wastewater treatment facility.

Midlands also offers two letters from Mr. Jim Stanton from Interstate Utility Sales and Mr. Anthony R. Combs from Combs & Associates, Inc. Mr. Stanton states in his letter that “while the steel or concrete structure may last longer than twenty years if properly maintained, the internals of a plant will require replacement before twenty years.” Further, Mr. Stanton clearly states that certain portions of the facility, such as the structure, may last longer than twenty years. The letter from Mr. Combs states that he “represent[s] the wastewater treatment plant equipment that [Mr. Parnell has] drawn and specified for the Bush River Wastewater Treatment Plant... [and] that a twenty year design life is our industry standard for this equipment.”

Considering the wastewater treatment facility is a combination of several different components, we find that a 25 year service life for the entire treatment plant is fair and reasonable and, therefore, adopt a depreciation adjustment of \$46,754.

(C) Chemical Expense

(1) Position of Midlands: Midlands, in its application proposed to adjust chemical expenses by \$5,000. See ORS Witness Barnette Testimony, P. 18, Audit Exhibit A-1, P. 5 of 5.

(2) Position of ORS: ORS proposes to adjust O&M Expense – Chemical expenses to reflect the projected expense after construction. In the As Adjusted calculation, ORS proposed no adjustment in the booked balance of \$10,639. Therefore, the calculation to get to the after construction expense is \$10,639 less \$5,000 (per application) which equals an

adjustment of (\$5,639). See ORS Witness Barnette Testimony, P. 18, 4-8. Audit Exhibit A-1, P. 5 of 5.

(3) Decision of Commission: The Commission finds an adjustment for chemical expenses is reasonable and consistent with the use of a sequential batch reactor. The Commission adopts an adjustment of (\$5,000) as the chemical expense adjustment following implementation of Phase-II of the increase.

(D) Property Taxes and Gross Receipts Tax

(1) Position of Midlands: Midlands proposes a \$5,000 increase in taxes from During Construction to After Construction.

(2) Position of ORS: ORS proposes to adjust Taxes Other Than Income to reflect an increase in property taxes and Gross Receipts tax in the After Construction Phase. This adjustment is based upon Midlands' estimated amount for taxes in the After Construction Phase. Gross Receipts taxes on the proposed increase would equal \$272. MUI proposes a \$5,000 increase in taxes from During Construction to After Construction. ORS proposes a change of \$6,904 from As Adjusted to After Construction Taxes Other Than Income.

(3) Decision of Commission: The Commission finds an adjustment for other taxes in the After Construction phase is reasonable and adopts adjustments to reflect an increase in property taxes of \$5,000 and an increase in gross receipt taxes of \$283.

(E) Utilities

(1) Position of Midlands: Midlands proposes an increase in the After Construction amount for utilities expense in the amount of \$20,000.

(2) Position of ORS: ORS proposes to adjust O&M Expenses – Utilities expense to reflect the change in amount from the As Adjusted balance to the After Construction amount as proposed by MUI. This is an adjustment from per books of \$40,963 to \$60,000 per application or \$19,037.

(3) Decision of Commission: The Commission concurs with the Company's calculation of the adjustment for an increase to utilities expense after construction (Phase II) in the amount of \$20,000.

(F) Insurance Expense

(1) Position of Midlands: Midlands proposes to increase insurance expense in Phase II in the amount of \$10,000.

(2) Position of ORS: ORS proposes to adjust O&M Expenses – Insurance expense to reflect the change in amount from the As Adjusted balance to the After Construction amount as proposed by Midlands. This is an adjustment from As Adjusted of \$73,699 to \$98,000 as proposed in the application or \$24,301.

(3) Decision of Commission: The Commission finds the Company's adjustments and manner in arriving at these adjustments to be reasonable. The Commission allows the Company's recommended adjustment to insurance expense in the amount of \$10,000 for after construction (Phase-II).

(G) Interest Expense

(1) Position of Midlands: Midlands' application for after construction operation includes interest of \$40,485.

(2) Position of ORS: ORS proposes to adjust Interest Expense from As Adjusted to the After Construction amount as proposed by Midlands in its application. The interest expense includes interest on customer deposits and interest expense on the new plant. This adjustment is calculated as follows: Interest After Construction per application of \$40,485 less Interest on Customer Deposits As Adjusted of \$2,051 equals the adjustment of \$38,434. ORS' calculation reflects total interest per application. See ORS Witness Barnette Testimony, P. 19, ll. 3-7, Audit Exhibit A-1, P. 5 of 5.

(3) Decision of Commission: The Commission finds that the interest synchronization method of calculating Interest Expense should be used. The Commission also finds that a 50% Debt/50% Equity capital structure should also be used since it is more representative of a normal capital structure. Utilizing the Company's allocated Rate Base, including sewer plant upgrades in Phase II, a 50% Debt/50% Equity capital structure, and an embedded cost of debt rate of 5.65% produces annualized Interest Expense of \$46,078. The Commission allows Interest Expense in the amount of \$46,078 After Construction (Phase-II).

(H) Professional Fees

(1) Position of Midlands: Midlands proposed an adjustment in its application to reduce Professional Fees by (\$50,000) during Phase-II (After Construction).

(2) Position of ORS: ORS did not address this adjustment.

(3) Decision of Commission: The Commission finds that General and Administrative Expenses should be decreased by (\$50,000) as proposed by Midlands to reflect Professional Fees as adjusted for Phase-II (After Construction).

(I) Income Taxes

(1) Position of Midlands: Midlands proposes to increase income taxes in the amount of \$6,238 to adjust income taxes After Construction (Phase II).

(2) Position of ORS: ORS proposes to adjust income taxes associated with the After Construction Proposed Increase in the amount of (\$34, 439). See ORS Witness Barnette Testimony, P. 19, ll. 8-10. See Audit Exhibit A-3, Computation of Income Taxes for details.

(3) Decision of Commission: The Commission agrees with both Midlands and ORS that the income taxes associated with the proposed increase should be adopted After Construction. However, the Commission finds the adjustment to be (\$15,608) based on our findings herein.

11. The Commission finds that an operating margin of 15.79% in Phase-I and 13.84% in Phase-II is just and reasonable and results in just and reasonable rates to charge for the services offered by Midlands.

12. The level of operating revenue required for Midlands to have an opportunity to earn a 15.79% operating margin under Phase-I rates is found to be \$1,342,506. The level of operating revenues required for Midlands to have an opportunity to earn a 13.84% operating margin under Phase-II rates is found to be \$1,379,071.

The following table indicates (1) Midlands' gross revenues for the test year after adjustments approved herein, under the proposed Phase-I rate schedule; (2) Midlands' operating expenses for the test year after accounting and pro forma adjustments and

adjustments for known and measurable out-of-test year occurrences approved herein; and
(3) the operating margin under the proposed Phase-I rate schedule:

TABLE B

After Phase-I Increase

Operating Revenues	\$1,342,506
Operating Expenses	<u>1,133,311</u>
Net Operating Income/(Loss)	\$ 209,195
Add: Customer Growth	<u>2,816</u>
 TOTAL INCOME FOR RETURN	 <u>\$212,011</u>
Operating Margin	<u>15.79%</u>
(Interest Expense For Operating Margin)	<u>\$ 0</u>

In order to meet the income requirement for the opportunity to earn an operating margin of 15.79%, Midlands will require additional revenues of \$389,057. This amount of additional revenues represent the increase in Midlands proposed rates and charges.

The need for the Phase-II increase has been justified by Midlands. We hold that ORS must conduct an audit of such plant expenditures and report back to this Commission, prior to the Phase-II rate increase going into effect. This will be discussed further below, along with other conditions that must be met before the Company may put the Phase-II increase into effect.

Additional revenues of \$36,564 are appropriate for Phase-II of the increase, for total operating revenues of \$1,379,071. Total operating expenses for Phase-II are \$1,145,289. We hold that all accounting adjustments from Phase-I will carry over into Phase-II. Total operating margin for Phase-II is 13.84%, considering interest expense of \$46,078. This may be calculated as follows:

TABLE C

After Phase-II Increase

Operating Revenues	\$1,379,071
Operating Expenses	<u>1,145,289</u>
Net Operating Income/Loss	\$ 233,782
Add: Customer Growth	<u>3,147</u>
 TOTAL INCOME FOR RETURN	 <u>\$ 236,929</u>
 Operating Margin	 <u>13.84%</u>
Interest Expense for Operating Margin	<u>\$ 46,078</u>

13. The Commission finds the increase in tap fees should be approved.

By its Application, Midlands requested to increase its customer tap fees from \$250.00 per SFE to \$500.00 per SFE, an increase of 100%. Midlands asserts that tap fees have not increased since the Parnell family has owned Midlands and that the increase in tap fee is necessary to recapture the plant investment.

ORS' position is that Midlands originally did not provide any cost justification for the proposed increase in customer tap fees and had not included in its application an exhibit setting forth all cost criteria justifying the tap fee. ORS initially asserted that Midlands had failed to comply with 26 S.C. Code Regs. 103-512.4.A.0 which requires that proper cost justification include labor costs, material costs and miscellaneous costs. At the rate increase hearing, ORS witness Hipp testified that ORS had subsequently received information from Midlands justifying the increase in tap fees and that she was satisfied with Midlands' justification.

The Commission finds that Midlands has complied with Commission regulations and has provided adequate information justifying the increase in tap fees. Tap fees are booked as Contributions in Aid of Construction (“CIAC”) and are included as a deduction from rate base. The Commission approves the increase in tap fees, but finds that the hearing record does not support the proposed increase in plant expansion and modification fees. However, the Commission will also increase Plant Expansion and Modification Fees from the currently approved \$250.00 to \$500.00. This should provide a contribution toward recovery of capital costs being incurred by the Company.

14. The current performance bond of Midlands is insufficient and does not meet the requirements of S.C. Code Ann. Section 58-5-720 (Supp. 2004).

S.C. Code Ann. Section 58-5-720 (Supp. 2004) was amended in May 2000 and increased the required amounts of performance bonds to a minimum of \$100,000 and a maximum of \$350,000. Thereafter, the Commission’s regulations were amended to provide for determining the amount of bond required by each utility. 26 S.C. Code Regs. 103-512.3.1 (Supp. 2004) was amended to provide that the amount of the bond should be based on the total amount of certain expense categories.

ORS witness Hipp provided testimony concerning the performance bond filed by Midlands. According to witness Hipp, Midlands has on file a performance bond with a face amount of \$50,000. The performance bond is secured by a personal financial statement of Mr. Keith Parnell, President of Midlands. Witness Hipp opined that the performance bond is insufficient because it does not meet the statutory amount required for the performance bond. Further, Ms. Hipp testified that that the surety filed to support

the performance bond is insufficient because (1) the amount of the surety does not comply with the requirement of 26 S.C. Code Regs. 103-512.3.1 (Supp. 2004); (2) the financial statement does not accurately depict the net worth of the surety as required by 26 S.C. Code Regs. 103-512.3.2 and 103-512.3.3; (3) the real estate indicated on the financial statement is in the name of another person and there is no documentation indicating authorization to pledge the real estate as part of the surety; and (4) the same financial statements and surety are used to secure performance bonds of Midlands' sister companies BRUI and DSI. On March 17, 2005, Midlands filed a late filed exhibit consisting of an affidavit of Mary G. Parnell representing that Lot 25, Section B, Rice Lane Plat Book 23, P. 78, Edisto Beach, Colleton County, South Carolina may be shown for surety and bond as necessary for DSI, BRUI, and Midlands. Mary Parnell in the affidavit represents that the lot is not now mortgaged, pledged or otherwise hypothecated. No appraisal identifying the fair market value of this property has been provided to the Commission.

Witness Hipp calculated that an appropriate bond for Midlands based upon the criteria contained in 26 S.C. Code Regs. 103-512.3.1, would be \$350,000. ORS Witness Hipp Direct Testimony Pp. Pp. 6-8 and Hearing Exhibit 13, Exhibit DMH-2.

DSI witness Parnell testified that Midlands had complied with the Commission's requirements concerning the performance bond. Keith G. Parnell Rebuttal Testimony, P. 2. Upon review of this issue, however, we find that Midlands' bond does not meet the statutory requirements of S.C. Code Ann. Section 58-5-720 (Supp. 2004). The statute requires a minimum bond of \$100,000 up to a maximum of \$350,000. The requirement of

the performance bond is to protect the public and to insure that the utility provides adequate and proper service.

The Commission finds a \$100,000 bond to be required for Midlands and hereby waives that portion of Regulation 103-512.3.1 which requires that the amount of bond be based on, but not limited to, the total amount of certain categories of Company expenses for twelve months. Commission Regulation 103-501.3 states that in any case where compliance with any of the rules and regulations introduces unusual difficulty, such rules or regulations may be waived by the Commission upon a finding by the Commission that such waiver is in the public interest. Considering the present financial position of the Company and considering the fact that the Company has had difficulty in the past in obtaining a surety bond, we believe that setting the bond in the amount recommended by ORS, which is in line with the cited portion of the Commission regulation, is going to introduce unusual difficulty for the Company in complying with that portion of the regulation. Further, the waiver of the stated portion of 103-512.3.1 is in the public interest since it allows the Company to more easily transition to a bond amount in line with the statutory language found in Section 58-5-720. The waiver should be granted. Midlands must comply with the bonding requirement by the earlier of November 29, 2005, or completion of construction of any of its new treatment facilities. The Commission will review bonding requirements if Midlands merges with any of its sister companies.

15. The Commission finds that Midlands should review all customer deposit accounts and, if the account is found not to meet the deposit retention criteria indicated in 26 S.C. Code Regs. 103-531.5, then each deposit should be adjusted/refunded with the

proper accrued interest to each customer. Midlands shall also review all deposit customer accounts and adjust/refund proper accrued interest for those accounts where it is acceptable to continue to retain the deposit.

ORS recommended that Midlands review its customer deposits and make adjustments to comply with Commission regulations and Commission Orders. ORS asserted that the Commission, under Order 2003-593 dated October 2, 2003, adjusted the interest rate for customer deposits from 8% to 3.5% effective January 1, 2004. Interest for customers in which Midlands retained deposits prior to December 31, 2003, should be due and payable at 8%. According to the books and records of Midlands, the customer deposit account had a balance of \$56,587 as of December 31, 2003. ORS recommended that Midlands should review all customer deposit accounts by the close of fiscal year 2004-2005 and, if deposits for any customers are found not to meet the deposit retention criteria indicated in S.C. Code Regs. 103-531.5, then the deposits should be adjusted/refunded with the proper accrued interest to the respective customers. Midlands shall also review all deposit customer accounts and adjust/refund proper accrued interest for those accounts where it is acceptable to continue to retain the deposit. Accrued interest on customer deposits is payable to each customer at least every two years and at the time the deposit is returned. ORS asserted that due to the length of time that Midlands has retained some customer deposits, Midlands should be required to adjust/refund proper interest at both the 8% and 3.5% interest rate.

The Commission finds that Midlands shall comply with the Commission's Order 2003-593 and adjust the interest rate for customer deposits from 8% to 3.5% effective

January 1, 2004. Midlands shall calculate interest at the rate of 8% for those customer deposits which Midlands has retained prior to December 31, 2003. Midlands concurs with the recommendations of the ORS, and Midlands shall review all customer deposits and adjust/refund proper accrued interest to all accounts. If the account does not meet the deposit retention criteria, then Midlands shall adjust/refund each deposit plus proper accrued interest to the customer. Midlands shall also adjust/refund proper accrued interest for those accounts where it is acceptable to continue to retain the deposit. Midlands shall refund accrued interest on customer deposits at least every two years and at the time the deposit is returned.

16. The Commission finds that Midlands should maintain its books and records in accordance with the NARUC Uniform System of Accounts, as adopted by this Commission.

Midlands witness Parnell testified that DSI is working to maintain its books and records under the NARUC Uniform System of Accounts and is in the process of making changes in order to bring Midlands' books and records into compliance with the NARUC Uniform System of Accounts.. The Commission's rules and regulations require sewerage utilities to use the NARUC Uniform System of Accounts. Keeping books and records in compliance with NARUC's Uniform System of Accounts will not only mean compliance with 26 S.C. Code Regs. 103-517, but will also make regulatory audits easier and less burdensome. ORS requested that Midlands be required to maintain its books and records under NARUC's Uniform System of Accounts. We agree that Midlands should be maintaining its books and records under the NARUC Uniform System of Accounts as

required by the Commission's regulations, and we find that Midlands should be in compliance with this requirement by the end of Phase-I.

After considering the Midlands' testimony in this case, it appears that Midlands personnel lack understanding of our Rules and Regulations, for whatever reason. We encourage Midlands to study the Commission's Rules and Regulations more carefully, and attempt to gain a better understanding of them. Further, we urge Midlands to seek help from personnel at the Office of Regulatory Staff when appropriate in this endeavor.

CONCLUSIONS OF LAW

Based upon the Findings of Fact as contained herein and the record of this proceeding, the Commission makes the following Conclusions of Law:

1. Midlands is a public utility as defined in S.C. Code Ann. § 58-5-10(3) (Supp. 2004) and as such is subject to the jurisdiction of this Commission.
2. The appropriate test year on which to set rates for Midlands is the twelve month period ending June 30, 2004.
3. Based on the information provided by the parties, the Commission concludes the appropriate rate setting methodology to use as a guide in determining the lawfulness of Midlands proposed rates and for the fixing of just and reasonable rates is operating margin.
4. For the test year of June 30, 2004, the appropriate operating revenues, under present rates and as adjusted in this Order, are \$953,449, and the appropriate operating expenses, under present rates and as adjusted in this Order, are \$1,001,573.

5. We conclude that Midlands has demonstrated a need for the here-in approved rate increase. We further conclude that Midlands has demonstrated the need for the two-phase increase in rates proposed in the application. Midlands has provided justification for an increase beyond the Phase-I rates as additional known and measurable expenses have been identified. After Phase-I of the rates, Midlands should have an operating margin of 15.79%. We conclude that an operating margin of 15.79% is fair and reasonable and results in rates which are just and reasonable. Likewise, we believe that an operating margin of 13.84% is fair and reasonable, and results in rates which are fair and reasonable for Phase-II of the rate increase.

6. In order for Midlands to have the opportunity to earn the 15.79% operating margin for Phase-I and 13.84% for Phase-II found fair and reasonable herein, Midlands must be allowed additional revenues of \$389,057 and \$36,564, respectively.

7. An increase from \$250.00 to \$500.00 is approved for tap fees and Plant Expansion and Modification Fees. The Company's proposed increase in Plant Expansion and Modification Fees from \$250.00 to \$2,000.00 is denied.

8. The rates as set forth in the attached Appendix A are approved for use by Midlands and are designed to be just and reasonable without undue discrimination and are also designed to meet the revenue requirements of Midlands.

9. Based upon the requirements of S.C. Code Ann. Section 58-5-720 (Supp. 2004) and of 26 S.C. Code Regs. 103-512.3.1 (Supp. 2004), Midlands shall post a performance bond of \$100,000 by the earlier of November 29, 2005, or completion of construction at any of its new treatment facilities.

IT IS THEREFORE ORDERED THAT:

1. Midlands is granted an operating margin for its sewer service of 15.79% for Phase-I and 13.84% for Phase-II.

2. The schedule of rates and charges attached hereto in Appendix A are hereby approved for Phase-I of the rate increase for service rendered on or after the date of this Order. Further, the schedule is deemed filed with the Commission pursuant to S.C. Code Ann. Section 58-5-240 (Supp. 2004). Prior to the Company implementing Phase-II of the rate increase, the Company shall undergo an audit by the Office of Regulatory Staff. Midlands must maintain its books and records according to the NARUC System of Accounts. ORS must perform an audit of Midlands prior to the Company implementing the Phase II rate increase. Audit guidelines shall mirror those this Commission approved on reconsideration of Order No. 2005-42 in Docket No. 2004-212-S. Midlands must be in compliance with DHEC regulations and requirements. Midlands must comply with the bonding requirements established by the Commission, and Midlands must have expended a minimum of \$1,168,850 in treatment plant upgrades and such expenditures must have been audited by ORS. Further, ORS must certify to this Commission that it has performed the required audit, and the results of that audit. Should the audit reveal non-compliance with Commission directives in this matter, the Company may not implement Phase-II of the rate increase until further Order of the Commission. In addition, DHEC must certify compliance of the Company with all of its requirements to the Commission. We cannot sufficiently stress the necessity for compliance with all directives of this Commission before implementation of Phase-II of the rate increase.

3. Should the schedules containing rates for Phase-I of the rate increase approved herein not be placed into effect within three months of this Order, Midlands shall require written approval from this Commission to place the rates into effect.

4. As discussed above, Midlands shall maintain its books and records in accordance with the NARUC Uniform System of Accounts as adopted by this Commission by the end of Phase-I.

5. Also, as discussed above, pursuant to and consistent with S.C. Code Ann. Section 58-5-720 and 26 S.C. Code Regs. 103-512.3 through 103-512.3.3 (Supp. 2004), Midlands shall post a performance bond with a face value of \$100,000 by the earlier of November 29, 2005, or completion of construction of any of its treatment facilities. The Commission will review bonding requirements if Midlands merges with any of its sister companies.

6. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

/s/
Randy Mitchell, Chairman

ATTEST:

/s/
G. O'Neal Hamilton, Vice Chairman

(SEAL)